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IN THE

Supreme Court of the United States

OCTOBER TERM, 1975

Nos. 75-1870, 75-1872

E. I. du PONT de NEMOURS AND COMPANY AND
CHRISTIANA SECURITIES COMPANY,
Petitioners,

SECURITIES AND EXCHANGE COMMISSION,
Petitioner,

vs.

RICHARD J. COLLINS, JR., LEWIS C. MURTAUGH,
TRUSTEE,
Respondents.

BRIEF OF RESPONDENT LEWIS C. MURTAUGH, TRUSTEE, IN OPPOSITION TO PETITIONS FOR WRITS OF CERTIORARI.

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OPINION BELOW.

The Opinion of the Eighth Circuit Court of Appeals Is Now Found at 532 F. 2nd 584.

QUESTION PRESENTED.

Has the Investment Company Act of 1940 created a safe haven as a matter of law so that a closed end Investment Company which has a fiduciary relationship with and controls an affiliated company can force a merger without allowing the

controlled company to share in vast benefits and increments its forced consent makes possible?

STATUTE INVOLVED.

In addition to the portions of the Investment Company Act of 1940 (15 USC § 80a-1 *et seq.*) set forth in the SEC Appendix (App. 113a-116a) and in the DuPont and Christiana Petition (pages 2-4), the following provisions of the Investment Company Act of 1940 are pertinent:

> "§ 80a-1.
>
> (a) Upon the basis of facts disclosed by the record and reports of the Securities and Exchange Commission made pursuant to section 79z-4 of this title, and facts otherwise disclosed and ascertained, it is found that investment companies are affected with a national public interest in that, among other things—
>
> * * * * *
>
> (3) such companies customarily invest and trade in securities issued by, and may dominate and control or otherwise affect the policies and management of, companies engaged in business in interstate commerce;
>
> * * * * *

STATEMENT OF THE CASE.

The majority Opinion's Statement of Underlying Facts (App. 45a), not objected to in the dissenting Opinion, is sufficient for this Respondent's purposes. This Respondent, a holder, as trustee, of 400 shares of DuPont, is more fully described below as Trustee for Emmanuel and Helen Steib, under Declaration of Trust dated 8/30/56. Nothing seems to be gained by insisting on the full description.

REASONS WHY THE WRITS SHOULD BE DENIED.

1. Certiorari Should Not Be Granted Because the Question Presented, as Set Forth by the Petitioners, Distorts the Facts in This Case, the Applicable Law, and the Basis of the Opinion of the Court Below.

The "Question Presented", as stated in the Petition of the Securities & Exchange Commission (hereafter described as SEC Petition), is deficient. It is phrased as follows:

> "The question presented is whether the Commission in approving a proposed merger of an investment company into an affiliated operating company, properly valued the investment company *essentially* on the basis of the market value of its assets *rather than* on the basis reflecting the substantially lower market value of its own outstanding stock." (Emphasis Supplied). (The same "rather than" dichotomy appears in SEC Petition 4 and 10).

If the stated question had stopped just before the "rather than" and had substituted "exclusively" for essentially, it would have been acceptable, even though it obscures the fact that the Commission's Opinion is based on its interpretation of the statute as a matter of law and is not a finding on a matter of evidence.

The DuPont-Christiana Petition, hereafter referred to as the D-C Petition, in its version of the "Question Presented" describes the disposition by the Court below as "substituting its own views for the judgment of the Commission in securities valuation, fairness, overreaching and protection of investors". Evidently the merging parties long for the safe harbor of a ruling based on evidence, but that is not what the Commission's Opinion is based upon. (App. 42a f. 5, 6 and text)

The D-C Petition though not stating in its "Question Presented" that the question was whether the market price of Christiana rather than the net asset value of its holdings should control, nevertheless, *unremittingly* argues that the market price

of Christiana was *the* chosen alternative by the Court below *rather than* the net value. The following quotations, all from the D-C Petition, will demonstrate that this is so. (All emphasis supplied).

Page 7—*"rather than"*

Page 9—heading *"Rather than"*

Page 10—"choice *between* market price and net asset value"

Page 11—"Its error was in assuming that the market price of Christiana common stock was *the* appropriate measure . . ."

Page 12—The Court of Appeals insisted that the terms *reflect* the market value of Christiana stock . . ."

Page 12 Footnote—"its conclusion that the market value of Christiana stock should *control* the merger terms. . ."

One of the objectives with respect to mergers set forth in the SEC report as related to the 1940 Act which was emphasized in the Opinion of the Court below (App. 59a) was to restore to mergers the standard of an arms length bargaining result which under conditions of common control was improbable in practice as state court decisions had developed. Chenery II (*SEC v. Chenery*, 332 U. S. 194 (1947) was an example of a ruling sustaining an even higher standard of fiduciary conduct under the Public Utility Holding Company Act of 1935 than the common law required, a situation where no detriment resulted but a fiduciary profited. It is a misbegotten citation when used to support lowering standards relating to fiduciary profiting and self-dealing. The Commission's Opinion, in effect, licenses closed-end investment companies which control affiliates to negotiate mergers for their own exclusive benefit. As the Court pointed out (App. 54a, f. 13), Section 1(a)(3) of the 1940 Act specifically indicates that the Act was directed to

prevent abuses in this situation. The SEC Petition finally winds up by saying "the Commission's interpretation effectuates the underlying policy of Section 17 to protect shareholders of investment companies from overreaching by affiliates" (page 17), but obviously Section 17(a), which prohibits transactions, is designed to protect all parties, and Section 17(b)(1) clearly has the same design, countering the particular abuse pin-pointed in Section 80a-1(a)(3) (p. 2 *supra* see also App. 54a f. 13).

Moreover, the whole idea of Christiana needing protection is absurd. By common consent the Commission and the Court below find that Christiana is in control of this situation. They cannot be forced into a merger on any terms to which they do not agree. The unreality of the argument that DuPont can possibly overreach Christiana is apparent. The only possible overreaching is that which can be done by a person in control who exercises that control to his own exclusive advantage. DuPont is in no position to overreach.

The Eighth Circuit Opinion (hereafter described as the Court Opinion) did not attempt to *substitute* the market value of Christiana shares *for* the *market value* of Christiana assets (more properly styled net asset value). The SEC Petition repeats this erroneous generalization with reference to the objectors position (page 6), though it reduces it later to the objectors seeking not all but a substantial share of the merger's increment. The Court's Opinion did insist on the necessity of taking Christiana share market value *as a factor* into account, *as well as its net asset value* (App. 54a, 56a, 57a, 58a, 61(a), 62a, 65a, 68a, 71a, 72a), and also took into account the market impact created by the increase of the floating supply of DuPont shares from 34,000,000 to 47.500.000 by reason of the release of pragmatically impounded DuPont shares held by Christiana, and the inevitable consequential increase in sales, especially and obviously by Wilmington Trust Company, strangling from lack of diversification in its over a billion dollars in illiquid Christiana shares

in fiduciary accounts (App. 88a, 89a, 90a).[1] The Court further refused to accept the Commission's concept that the merger terms were reasonable and fair as to DuPont because no detriment was incurred by DuPont or its shareholders (an assumption, by the way, that this Respondent denies and deals with later). The Court Opinion states "Lack of detriment is, like net asset value, just one factor to be considered in determining the reasonableness and fairness of a merger" (App. 72a, f. 22). The lack of benefit to DuPont, rather than an alleged lack of detriment, is certainly a reason for not entering into the proposed merger. Mergers are associated with some conceived benefit or increment to both merging parties.[2] That this concept should be utterly eschewed in this fiduciary context as a matter of law in favor of a controlling fiduciary is certainly regressive. The concept that a merger which is controlled on both sides, by one side, which automatically triggers fiduciary standards, can be so structured that the increment and other benefit from the merger goes entirely to the controller violates the principles set forth in *Pepper* v. *Litton* (1939), 308 U. S. 295, 306-307, relied on in the Court Opinion (App. 61a). This opinion, requiring terms such as would result from arm's length bargaining, is undoubtedly one of the most frequently cited in the whole area of fiduciary responsibilities in every context (in the 1943-1971 Shepard Citator there are over seven columns of citations). In *"Fair Shares In Corporate Mergers And Takeovers"*, Brudney and Chirelstein, 88 Harvard Law Review 297 (December, 1974), the authors strongly challenge the validity of a result in which the controlling side in a merger receives post-merger benefits

1. On trust diversification imperatives, see "Market Funds and Trust Investment Law", Langbein and Posner, Volume 1976, No. 1, American Bar Foundation Research Journal, page 1, at pages 3-21.

2. A comprehensive compilation of economic and legal considerations in connection with mergers generally is found in 88 Harvard Law Review 308, Footnote 33, in the article mentioned later in this section.

while the controlled side has to be content with having only pre-merger status (p. 311). The authors point out that no sharing in incremental values of the merger results in this situation, which is a violation of fiduciary principles.[3]

The Commission rejected all evidence as irrelevant, as the Court Opinion precisely noted in its forthright Section II (App. 51a). This evidentiary matter rejected included the expert reports and testimony introduced by the applicants (App. 17a, f. 38) and evidence introduced by the SEC staff and this Respondent (CA App. Index V and VI) and that attempted to be introduced by this Respondent (App. 41a, 42a, also f. 5 and 6 on 42a).

As the Court ruled (App. 51a, 53a, 54a), the Commission's issuance of an exemption in this context cannot be based solely on a ruling as a matter of law, but on evidence. The Court said, "The Section (17(b)) does not *limit* the considerations relevant to the approval of a merger to the preservation of the net asset value of the investment company" (App. 54a) (emphasis supplied). This is not to say that net asset value is not a factor as suggested by the SEC Petition's "Question Presented", and as is reiterated throughout the D-C Petition, but just that it is not, as a matter of law, an exclusive factor. In several other places in the Court's Opinion the Court makes it clear that it, in turn, is not creating a competing rule of law but is rejecting the rule of law stated in the Commission's Opinion which excludes all evidence (App. 54a, 68a, 86a, 90a).

A further criticism of the statement of the SEC "Question Presented" is the use of the term "market value of its assets" to upgrade, by suggestion, a dollar figure, the correct term for which is "net asset value". Net asset value is merely a figure obtained by multiplying any number of DuPont shares

3. The fact that the authors illustrate their point with a larger controller merging its controlled subsidiary into it does not detract from their theme that a fiduciary power center should not take all the increment from a merger.

held by any investment company (from one to thirteen and a half million here) by the current market *price*, not value, of its underlying assets. Christiana's accountants know better. See the numerous caveats in the proxy statement Exhibit (CA App. 715, 7, 8), pertinent parts of which, for the convenience of the Court, are in the Appendix to this Brief.[4] The point on the misuse of "market value" is rather thoroughly gone into in the Shapiro cross-examination (CA App. 474-81).

2. The Case Presents No Special or Important Questions and No Purpose Could Be Served by Remanding.

This case presents no apt occasion for granting certiorari within the principles set forth in Rule 19 of this Court (Considerations governing review on certiorari). Arguably, it might be different if the Circuit Court of Appeals had upheld the Commission's exemption order. In that event, to paraphrase the closing sentence of this Respondent's eleven-page Request for Hearing of October 25, 1972 (CA App. 90k), "The shareholders of DuPont, fixed in a web of interlocking directorates in probably the most obvious (and colossal, in terms of dollars) conflict of interest posture in corporate, legal and financial experience since the securities industry first came under mature control" could legitimately argue that this Court should review the matter. A half billion dollar enrichment of insiders in a merger in which they transfer control by way of relinquishment, and control both sides of the merger, is one which could legitimately call for close scrutiny at every court level. Since the Eighth Circuit has acted to prevent this peculiarly specific transaction, there seems to be no obvious reason for certiorari. DuPont and Christiana, after the Commission had (over their vigorous protests) granted a Request for Hearing of the now

4. This Respondent regrets belaboring the point as to the "Question Presented", and alleged equivalences, but casuistical extensions of sophistical assumptions are the kernels of these and several other argued difficulties in this matter.

Respondents, chose to execute an agreement to merger (CA App. 698). The Commission, therefore, had before it, and the Eighth Circuit also had before it, a single question, namely, whether the agreement authorized by the directors of the two companies should be granted an exemption or not. Neither the Commission nor the Court was in any position to do anything but vote this particular agreement up or down. The Applicants for Exemption did not apply for instructions or guidance, nor ask the Commission to make a determination as to what was a fair ratio, if the agreement in question was not fair, nor a motion to send the matter back for additional evidence as Section 43 provides. This is unlike many administrative proceedings, such as a rate-making proceeding or many court proceedings, such as a condemnation or even a public utility-holding company determination, where the Commission has to make the decision and can alter a proposal before it.

Assuming that the net asset value does not preempt all other considerations and that the market price of Christiana should have been taken into account, as well as the tremendous benefit of increased marketability, the tax free advantages which DuPont's consent affords, and weighing in the detriments, it is perfectly obvious that no finding based on the evidence would justify a ratio of 42-1 in benefits just considering the investment appreciation factor. In Appendix B to this Brief there is shown material which appeared on a single page of this Respondent's Appellate Court Brief (page 65), which sums up all the benefits and detriments in this merger. All of this is immaterial, apparently, if net asset value is to govern, but if any of them, including the "striking disparity" (App. 35a) are taken into account, the 2½% discount from net asset value, which was designed as a sort of catch penny inducement for shareholder votes (CA App. 457, 460, 585, 587) cannot possibly balance this situation. In other words, it would be impossible for the Commission to find as a matter of evidence that this transaction, *including the consideration to be paid and*

received, was reasonable and fair and not overreaching. Therefore, there is no occasion to remand the matter for further action by the Commission so far as this particular merger on these particular terms are concerned. This does not slam the door on another merger upon fairer terms, if Chistiana should want it. DuPont having consented to the present terms and being controlled, with its management anxious to seize the reins would obviously approve.

3. Certiorari Should Be Denied Because the Commission's Ruling Is Not Based on Established Principle and Strains and, in Fact, Ignores Part of the Law It Interprets.

The Opinion of the Court (App. 61a-67a) was convincing in rebutting the assertion that the Commission had established any rule or principle of law in any prior ruling, similar to the governing rule stated in this case, that the net asset value of a closed end investment company must be honored against all other factors. If this were so, a simple quotation would suffice to establish the rule's existence. Certainly the attorneys of record here for DuPont have top experience in this field and their "Factors to be Considered" letter of instruction (CA App. 768-774) is devastating to the present analysis by the petitioners of past Commission rulings. The most telling part of the "Factors" letter for this respondent's instant purpose is the portion quoted in Footnote 12 of the Court's Opinion (App. 53a) which includes, among other elements, market values and net asset values as factors in the Commission's rulings. The single most important sentence for our purpose is the closing sentence quoted in the Opinion Footnote, "No single factor has been considered determinative". Here the Commission's Opinion definitely does consider, as a matter of law, that the single factor of net asset value is determinative. In the "Factors" letter, the attorneys merely claimed that "the SEC has held net asset value relevant in valuing investment companies . . .", (CA App. 771) not conclusive. In the *Delaware Realty* case referred to in the "Factors" letter (CA App. 770), where the SEC accepted net asset value as a basis for a merger, the "Factors" letter said, "The rationale for this was that the parties to the merger had alternative means of recognizing net asset value without significant tax effect (1)". The footnote said, "Other similar cases considered by the SEC have involved little or no discount but have not expressed a specific rationale for this approach". The letter goes on to say that Christiana is taking the position that a Section 333 liquidation under the Internal Revenue Code is an alternative whereby it "presumably could achieve, with relatively little taxation, a liquidation in which its DuPont securities would be distributed directly to its shareholders" (CA App. 770). The following paragraph instructed the advisors "the report should indicate whether, on the assumption that the 30 day liquidation provisions would operate to Christiana's benefit here, du Pont would be justified in giving little weight to the market value of Christiana in the merger negotiations."

Apparently even students of the law find that not only is there no rule or principle as to net asset value controlling in a merger such as this which must pass scrutiny under Section 17(b) but actually find that some "cases suggest that fairness requires a sharing of the gains resulting from the merger", (*Fair Share In Corporate Mergers And Takeovers*, Brudney and Chirelstein, 88 Harvard Law Review 297, 310, 1974). In a footnote to the quoted statement the following appears:

> "The sharing requirement is sometimes found in opinions of the Securities and Exchange Commission dealing with the fairness of mergers under the Investment Company Act, 15 U. S. C. § 80a (1970). LaSalle St. Capital Corp., SEC Investment Company Act Release No. 6693 (Aug. 23, 1971); Talley Indus. Inc., SEC Investment Company Act Release No. 5953, (1969-1970 Transfer Binder) CCH Fed. Sec. L. Rep. ¶ 77,774 (Jan. 9, 1970); Townsend Corp. of America, SEC Investment Company Act

Release No. 4045, at 35-39 (Sept. 2, 1964); Atlas Corp., SEC Investment Company Act Release No. 2920 (Oct. 19, 1949). Compare Burco Inc., 15 S. E. C. 828, 832-33 (1944), with Iowa Interests Corp., 40 S. E. C. 927 (1961)."

Facing up to the fact that its analysis of prior Commission rulings may not serve as an adequate precedent for the legal ruling made by the Commission in this matter, the D-C Petition, on page 10, argues that even if this is a case of first impression, the Court should abjure its jurisdiction under Section 43 of the Act "to affirm, modify, or set aside such order in whole or in part" as regards matters of law. This is well trod turf and too little supported to justify a considered rebuttal at this stage beyond the treatment it received in the Court's Opinion (App. 73a, f. 25). Reference might also be made to "Judicial Control of Administrative Action". Jaffe (p. 576 et seq. "The correct relation of expertness to the scope of review").

However, there is a provision in Section 17(b), (1) constantly omitted in the Petitions and the SEC Opinion, which strongly militates against the Commission's ruling as a matter of law. The Commission, in its findings (App. 36a, 37a), does not find that the terms of the transaction, *"including the consideration to be paid or received . . ."* (Emphasis Supplied), which qualify the remaining factors to be considered. (Both Petitions similarly ignore this statutory factor). On the contrary, on analysis, the Commission's Opinion finds this very element lacking. The Opinion states "the questions presented are substantial and troublesome. This is not an easy case" (App. 17a). Later in the Opinion the Commission states, "This is not an easy case . . . Its difficulties . . . flow . . . from the *striking disparity between* the substantial benefits to be received by Christiana and the far more modest ones inuring to DuPont" (App. 37a) (Emphasis Supplied). As stated in *Willheim* v. *Murchison,* 342 F. 2d 33, 43 (2CCA) c.d., 382

U. S. 840 (1965), the 1940 Act was drawn with a great deal of specificity and should not be given a construction that strains its plain meaning (cited in App. 53a). The SEC, as amicus, supported the straining (and losing) side's interpretation.[5] No amount of expertise can overcome the dictates of a statute or remedy an administrative excess of a statutory warrant. One of the specifics under Section 17(b)(1) was that the Commission, *as a matter of law*, had to take into account "the consideration to be paid or received". Had due consideration been given to this, the Commission might not have created law which specifically sanctions, as a matter of law, a striking disparity of dollar increments and other benefits. See Appendix II attached hereto where the relative benefits and detriments are tabulated.[6]

4. The Market Price of Christiana is its Investment Value and a Sharing by DuPont in the Increment of Close to a Half Billion Dollars Is not Sharing in Christiana's Tax Savings As Contended by Petitioners As a Basis for Certiorari.

The discount from net asset value at which Christiana sold does not *result from* the tax burden on Christiana (SEC Petition 4, 7; D-C Petition 11), and the SEC Opinion never said it did, although it did state that avoiding certain taxes was an advantage to Christiana (App. 11a). The statement on page 4 of the SEC Petition that, apparently, the discount of 7.2% of the dividends received by Christiana from DuPont, which

5. See also the recent case of *United States* v. *National Association of Securities Dealers* (1975) 95 S. Ct. 2427, where the court rejected (Page 2439) a decision below (emphasis supplied) *"reflecting an expansive view* of Section 22(d)" of the 1940 Act, although the decision below served the statutory purpose of protecting the net asset value of open-end investment fund shares.

6. The D-C petition refers to the case of *Harriman* v. *DuPont,* 411 F. Supp. 133, and includes a 4-page quotation from it in an Appendix. To preserve the unity of this brief, we comment on this case in Appendix III. The court below referred to this case in footnote 18 (App. 66a) and footnote 23 (App. 72a).

resulted from the intercorporate dividend tax, was one of the elements (of a total of two) responsible for the discount from Christiana's net asset value does not stand analysis. On the announcement date, April 28, 1976, that consideration was being given to a merger, DuPont was selling at 168.25 and Christiana was selling at 147, although it held 1.15 shares of DuPont for each share of Christiana outstanding. Christiana was distributing to its shareholders its post-income tax dividend, about half the 15% dividend excess over that which a share of DuPont received. How, in all reason, could a 7½% *higher* dividend explain a $21.25 lower price, just on a share for share comparison, of one share of DuPont versus one share of Christiana, forgetting that Christiana had 1.15 shares of DuPont for each share outstanding? The SEC Opinion recognized this and paused to speculate as to why the price of Christiana shares wasn't 7% higher than DuPont, in view of its net yield in that amount over the yield for DuPont shares (App. 12a, 23a, f. 44).

The *only* other apparent cause for the market discount from net asset value of Christiana shares which the SEC Petition relies upon to furnish a completion of the explanation of the discount was the unrealized appreciation on Christiana's DuPont stock over its carrying value on Christiana's books (SEC Petition 4) which would be subject to capital gain tax if Christiana sold. This is likewise no reason for the discount which would be wider if this was a potential. Right off, a 30% capital gain tax applies to corporations. Christiana would not only have suffered a capital gains tax, but its shareholders would have ordinary income tax were Christiana to pay out the net proceeds. The discount in this situation should have been 50% to 70%. The utter improbability of Christiana selling its DuPont shares was such that this factor could not and did not at all explain the discount from net asset value.

The D-C Petition attempts at page 11 to add the capital gain tax in the event Christiana assets were distributed in a taxable

liquidation as a factor in explaining the price. This factor has no logical connection with the market discount as it did not affect purchasers, except affirmatively. The SEC Petition rightly ignored it. (On the other hand, the D-C Petition does allow a thin trading market as a factor in the discount. This is what the accountants keep warning about (See Appendix I).[7]

The fact of the matter, as the Commission's Opinion notes, is that "Christiana, like most closed-end investment company issues, has long tended to sell at a discount from net asset or liquidation value" (App. 5a). The Court Opinion (App. 86a and 87a), in recognizing the factor of the intercorporate dividend tax and unrealized capital gain tax as merely "affecting", not explaining, the market price of Christiana, merely stated that this was not a reason to ignore Christiana's market value. In Footnote 36 (App. 87a), the Court affirms the Commission's statement, above quoted, as to the endemic nature of the closed-end discount from the net asset value of closed-end funds' portfolios. It cites, among other authorities, *"Discounts and Premiums on Closed-End Mutual Funds; a Study in Valuation"* by Kenneth J. Boudreaux (May, 1973, 28 Journal of Finance 515-522). That author states categorically, "the market price of a close-end fund can fairly confidently be considered to represent the best estimate of the funds true value at each point in time" (p. 521). A thorough reading of the Boudreaux article does not disclose that the author assigns the reason for *any* part of the closed-end funds market discounts from net asset values to tax considerations.

In a recent issue of "Business Week" (June 28, 1976), at page 86, there is an article about a proposal to establish regular payouts from closed-end mutual funds, invading principal if necessary, in an attempt to encourage investors who at present rely on just the income of the funds. There was some

7. (But see the Business Week quotation, *infra*, page 16, as to multi-million dollar closed end funds widely traded on the NYSE and selling at large discounts from net asset value).

difference of opinion in the mutual fund industry as to such a proposal. The article says:

> "But the doubters are watching closely to see whether the prospect of large, regular distributions will reduce the large discounts from net asset value at which almost all closed-end funds usually sell.
>
> Nobody really knows why these funds do sell at such substantial discounts. For example, the $640 million Tri-Continental Corp. and $470 million Lehman Corp., the two largest, are both trading at the moment on the New York Stock Exchange at around 26% below net asset value. The Assn. of Closed-End Investment Companies has funded a study at the Wharton School of the University of Pennsylvania to discover the reasons, but advance reports suggest it may be inconclusive."

The testimony of Charles Townsend of Morgan Stanley to the same effect is set forth in the Court's Opinion (App. 57a, f. 14). Edward Townsend of the First Corporation was even more emphatic (CA App. 319) that the net asset value of Christiana shares was no index of its value, but that Christiana's price was its value. Later he reiterated that Christiana shareholders were not holding DuPont shares underpriced and that Christiana shares were not underpriced (CA App. 332). Even Mr. Shapiro testified to the same effect (CA App. 481).

The argument for a sharing in the benefits of this "consensual" transaction is not a disguised plea for sharing in tax benefits. In fact, it implies in one sense that Christiana shareholders, while reaching for the near half billion dollar benefit for the exclusive enjoyment of its shareholders, will fall short to the extent that the market is depressed by the increase of nearly 40% in the floating supply of DuPont shares above the 34,000,000 of DuPont shares now floating. Christiana shareholders will be richly rewarded in principal and income increment and marketability in any event despite market impact but there will be no compensating features to the detriment suffered by the other DuPont shareholders. Christiana shareholders will get the theoretical increment of close to a half billion dollars minus the market detriment from the increase in the floating supply brought to market. DuPont shareholders who sell will get their pre-merger price minus the currently effective market detriment. Allowing for this is not sharing at all. It is only an adjustment to preserve the status of DuPont shareholders relative to the floating supply before the merger, the barest requirement of justice and fairness, when DuPont and its shareholders must consent.

5. Certiorari Should Be Denied Because This Case Is Poorly Suited to Enable the Court to Establish Any Basic Principle Rationalizing Law or Economics.

The SEC Petition rushes in "where angels fear to tread" by its universal generalization that the discount from net asset value results from two tax factors, as above discussed. This furnishes a q. e. d. to the following statement:

> "When one reads the economic literature, one realizes almost at once that there is a hiatus between the SEC's pretensions as to what it is accomplishing and the economists' appraisal of what the SEC is accomplishing. The economists almost totally ignore the SEC, treating it like some imperfection in a communication system, like some static. Its role is obviously not of fundamental importance to their thinking."

This paragraph is from the first page of an article by Professor Homer Kripke in Volume 31, The Business Lawyer, 293 (ABA, 1975). After giving importance to the article by denominating it a "Bicentennial Paper", the following statement appears:

> "The Editors of The Business Lawyer are pleased to present, as a Bicentennial contribution, a seminal article by a distinguished author which examines both with candor and with an eye to the future an important aspect of corporation law."

The author more modestly entitles his study as "A Search for a Meaningful Securities Disclosure Policy".

With respect to granting certiorari, the Court may consider that this may not be the ideal case for this Court to rationalize a detente, if not a rapprochment, with economists, graduate market scholars and econometricians. For one thing, this Respondent has had no scholastic economic education, and though he has gleaned much information in the last four years, the result has been mainly to gain respect for horizons of which the law has barely become aware or worked out a coherent concordance, or even accomodation, in principle.

Some dimensions of the interdisciplinary condition can be grasped from Section III of Professor Kripke's study, entitled "Some Aspects of the Economics of the Securities Market", Kripke, *supra,* at 305-12.

Obviously the Eighth Circuit, searching for illumination as far as the true situation could be discovered by a rounded analysis, as opposed to a preemptive legal ruling, sought purely professional assistance in the economic field. There is no more occasion to criticize the Court for this than for this Respondent to apologize for referring to the Kripke article. Moreover, a close reading of both Petitions discloses no reference to any part of the Opinion, or to Dean Upson's report, to which they object. At its strongest, this is merely an example of injury without damage and hardly warrants certiorari.

6. Certiorari Is Not Warranted Since the Court's Finding of Probable Market Impact as a Detriment Is Strengthened and Made a Fortiori by Several Considerations.

The D-C Petition (Page 16, f. 8) incorrectly predicates error in the Court finding of market impact as a factor to be taken into account. The Commission's Opinion expressly agreed with this Respondent that increased supply would, all other things being equal, lower prices (App. 27a). It simply refused to go

into the matter (App. 26a). The Commission did state that lower prices would attract the attention of buyers (App. 29a) but it refused to have the record enlarged to provide an understanding of how many sellers might be involved, and taxed this Respondent for not producing a schedule. As the Court Opinion noted, the burden was on the Commission (App. 54a, 51a, f. 8). This Respondent attempted to make more evident the probabilities of market impact, but the Commission stated that this was pointless and irrelevant (App. 36a, 42a). The Commission finally cut the knot by stating the net asset value concept overcame any possible market impact detriment (App. 32a-33a) and, as stated, finally held as a matter of law that market impact was irrelevant. Naturally the Court below wanted some orientation on this subject, and utilization of Dean Upson was just to keep the Court, in its Opinion to be written, from uttering some gauche generalization in a field in which it had little background. The SEC's position was that background wasn't necessary since it had decided the issues as a matter of law.

Bolstering the foundation of the Court's Opinion's finding of error in the Commission's failing to give any weight to the factor of occasional detriment to DuPont shareholders (App. 90a) is the fact that the Court Opinion erroneously assumes that "the merger agreement, however, provides that once a year an underwritten offering of $25,000,000 in the then current market value of such shares can be made. At the average price of $165.00 in the first 6 months of 1972 this would approximate 153,000 shares" (App. 90a, f. 38). The Court Opinion's error in regard to secondaries is twofold; the first, and least important, is that the merger agreement is not the instrument which refers to underwritten offerings that reference is found in the agreement regarding registration (CA App. 836-8) which was considered after the agreement to merge in principle had been made in July of 1972. Disclosure of its terms in general was made by the introduction into evidence of the then current draft of the

registration agreement by this Respondent as Murtaugh Exhibit 15 (CA App. 833). The second, and more significant, error in the Court's Opinion (App. 90a, f. 38), but one which only fortifies its conclusion, is that the reference to the underwritten offerings of $25,000,000 once a year is not correctly stated to be the floor but the ceiling for such underwritten offerings. In other words, the registration agreement provision is that the underwritten offering shall not be less than $25,000,000 (CA App. 837), but it can be as much more as the former Christiana shareholders choose to demand. In fact, DuPont is required to notify other shareholders having registration rights so they may add on (CA App. 837).

A further point supportive of the Court Opinion is the fact that DuPont has no power to refuse to register its shares for underwritten secondary offerings annually (CA App. 837) unless it would interfere with its current financing (CA App. 838). The reason secondary offerings can sometimes be effected with surprisingly short term adverse market effects is that the company can exercise its best judgment as to when, in its interest and the interest of its shareholders, the adverse effects will be offset by other factors (CA App. 198). With the discretion solely in the hands of individual Christiana shareholders as to where their best interests lie, the potential for damage is greatly increased and the remaining shareholders of DuPont are hostages to fortune.[8]

8. On direct examination Charles Townsend of Morgan Stanley testified on the basis of an assumption of 10% of DuPont Company stock, 4.7 million shares, being marketed over a period of five years. As to the time span of periodic market effects following successive issues, he testified (CA App. 199) "It would be difficult to tell. Maybe a month, maybe two months, maybe even three months, *depending on the market conditions at the time*, the way in which the underwriting has been done. We would not want to recommend that sellers of du Pont stock *overtax the market at any particular time*, and *the size of the issue would have to be gauged accordingly*". (Emphasis supplied) Neither Morgan Stanley nor DuPont have any controlling thing to say about the *size* of an issue, or whether it would overtax the market at any particular time

(Continued on next page)

Of course, the size of the issue and its market impact, which might be well called minimal if limited to 153,000 shares, as the Court assumed, cannot be so judged when it may be limitless, beyond DuPont's control, and must be above 153,000 shares. There is no limit, except in the disparate selling shareholders discretion to prevent overtaxing the market, which DuPont's Morgan Stanley witness warned against (CA App. 199). Furthermore, the Court Opinion is fortified by the consideration that the effect of repeated secondaries is naturally cumulative. This was strongly argued to the Commission and the record made by DuPont and Christiana in the General Motors divestiture case (*U. S.* v. *DuPont*, 177 F. Supp. 1 (N. D. Ill. 1959) was that sales of .7% a year over a 10 year period, which sales were postponable in bad years, and assuming that there was no adverse tax effect, would cause a continuous market depreciation of 10 to 15% in General Motors share prices. The Commission's opinion referring rather genially to the D-C assertedly contrary contentions in the General Motors case (CA App. 33a, f. 59) relies solely on the income tax burden under then existing law which might impel selling to pay taxes, a factor not present here, but the evidence in the record here was the D-C evidence, *assuming* pending tax relief measures were enacted, so that only the market impact of the continuous selling of 7% in .7% instalments of General Motors serially over a period of 10 years, postponable in bad years, was the key point, entirely neglected in the Commission's opinion and, in fact, overlooked in the Court's Opinion, but fully explored in the transcript and in the exhibits (CA App. 507-11, 793, 796d, 796e). (No contention has been made there would be endless waves or mindless torrents of selling. This could drive DuPont down 50%. A rational

(Continued from preceding page)

under the Registration Agreement (CA App. 836-8). Therefore, the assumptions in the witness' testimony as to detrimental market effects based on postulated good market conditions or a limited size of the issue and a gauging based on any DuPont Company interest as against the seller's view of their own best interest is fanciful.

balance could easily keep the discount at or near 10-15% as D-C contended). This Respondent, of course, strongly supports the Court Opinion in this case and submits that the point made in this and the next section of this brief merely bolsters the conclusion that "it follows that the Commission erred in failing to give any weight to the factor of an occasional detriment to DuPont shareholders" (App. 90a).

7. Company Detriments From Market Impact[9]

Two circumstances of possible detriment affecting the assets and earning power of DuPont itself should be mentioned and were pressed both in this Respondent's brief to the Commission and to the Court below. The first is that a depression in the price of DuPont stock might interfere with the use of its stock in acquisitions, or might require it to issue more shares than it otherwise would. See the article "Shenandoah Oil Ends Merger Talks with DuPont", Wall Street Journal, July 12, 1976, p. 6. See also Business Week item in July 29, 1976 issue, p. 54. The lowered price of DuPont apparently aborted this acquisition by stock when Shenandoah sought a larger number of shares than previously agreed to, is a lost opportunity affecting all DuPont shareholders, *including long term investors*. Companies with adequate information and good judgment are liable to be wary of a stock being acquired which has a large block selling or secondary overhang situation and certainly will want to renegotiate if the shares they expect to get drop in price. A second detriment to the company might be interfering with its equity financing. Though the registration agreement excuses

9. The distinction between market information which has no effect on a company's assets or earning power, and company information which does, is made and elaborated on in the first respect in *"An Initial Inquiry into the Responsibility to Disclose Market Information"*, Fleischer, Mundheim & Murphy, 121 U. of Pa. Law Review 798. The SEC Opinion asserts no company detriments and no contrary contention (App. 28a). The D-C Petition points this out (page 14). This section contradicts this statement.

DuPont from registering underwritten secondaries in any year in which, in the opinion of DuPont's investment bankers, such offering would interfere with the then current financing plans of DuPont (CA App. 838), this doesn't prevent before and, prospectively, after market effects from secondaries which may interfere with current financing. Furthermore, the additional requirement for registering shares twice a year for disposition other than in underwritten secondaries (App. 856), cannot be valued other than negatively in terms of active new floating supply. Additionally, as stated in a recent Supreme Court case, the tremendous growth of federal security law litigation which, of course, frequently involves asserted misrepresentations or omissions, of which DuPont may serve as a guarantor, the nuisance suit feature so often found, and (with reasonably grounded, or nuisance suits) discovery rights ancillary to securities litigation which may be collaterally very detrimental to a company. This case, *Blue Chip Stamp* v. *Manor Drug Stores* (June 9, 1975) 95 S. Ct. Rep. 1917, turned in part on these circumstances.[10]

Reflection on the matter emphasized in this late case draws attention to the fact that the constant registration statements

10. The remaining part was a reversal of an SEC supported construction of the 1934 Act. During the recently closed and previous term of this Court, several Opinions have been rendered, and certiorari has been granted in other cases, bringing into question the validity or scope of certain provisions of or interpretations of Section 10(b) of the Securities and Exchange Act of 1934 (15 U. S. C. § 78j) and Rule 10b-5 issued thereunder. One unsettled issue seems to revolve around whether Section 10(b) which does not use the word "fair", deals only with misrepresentations, concealment, manipulation or fraud, and whether, without these factors, fairness is an issue. These very current developments have nothing to do with this case, where fairness is a statutory prerequisite under Section 17(b)(1) of the 1940 Act. The Commission's Opinion recognizes a Federal fairness standard has been stipulated, formulated in large measure because of the inadequacies of state law (App. 19a). The Court Opinion convincingly agrees, quoting from the legislative history (App. 58a-61a). Legislative history is uniquely incorporated by reference in Section 1 of the 1940 Act (15 U. S. C. § 80(a)1).

may give rise to shareholder suits in connection with current or prior registration statements because the circumstances of an upcoming registration by insiders was not disclosed (See *Birdman* v. *Electro-Catheter Corporation* (E. D. Pa. 1973) CCH Fed. Sec. Law Rep. Section 93, 934, dealing with the failure to disclose potential market impact on a contemplated sale of share by insiders.) Wilmington Trust Company with 56% of the new stock, and many interlocking directors of DuPont, with all sorts of company and marketing information, and possibly conflicting duties as trustee, is an insider *par excellence*. To avoid danger constant warning about possible registrations beyond DuPont's control will certainly be market depressants inimical to the interests of the company and all of its shareholders.[11]

CONCLUSION.

In an era of great sensitivity to conflicts of interest and fiduciary responsibility, it is interesting to note that the Commission's Opinion never once mentions either term (except in footnote 36, App. 15a, where it refers to Wilmington Trust Company's fiduciary responsibility as to its trusts). Because a fiduciary relationship is so patent is no reason to ignore it.

Typically, a gross enrichment of a fiduciary in a self-dealing transaction is a badge of a breach of a fiduciary obligation with-

11. It is clear from the Opinion of the court below (App. 51a, 52a ff. 8, 9) that the Memorandum Opinion of the Commission denying the "Supplemental Petition of Lewis C. Murtaugh for Rehearing, Including Motion for Leave to Adduce Additional Evidence", which Memorandum Opinion is found at pages 40a-43a in the Appendix, was an important factor in clarifying the Commission's position that a rule of law was involved which made immaterial any evidence as to market impact or intentions to sell or probability of sales and also of evidence on any aspect was relevant. To grasp the scope of the denial of the Motion, it would be helpful to read the rather extensive Supplemental Petition and Motion of this respondent which is found in the Court of Appeals Appendix at pages 131-143. Additionally, of course, this constitutes a rather complete analysis and criticism of the Commission's Opinion filed about five weeks after it was rendered.

out further evidence. The only defense here is sophistry built on a misstatement designed to persuade that a share of Christiana is, in reality, 1.15 shares of DuPont. The asserted "reality" is denied in the opinion below (App 57a). A statutory madrigal of cancellation and conversion cannot equal transubstantiation. At best, it can beg the question (see footnote 4 *supra*).

The conceded control (App. 41a, f. 3) and active participation in DuPont affairs of Christiana's directors and large holders of Christiana on DuPont's Board (App. 75a, 76a, 85a. 86a), the fact that neither of the two independent directors was utilized (App. 76a), the fact that McCoy, one of the negotiators, is also a director of Wilmington Trust Company (App. 75a), which will succeed Christiana as the largest holder of DuPont shares and which, in turn, has counter-fiduciary responsibilities, all lead to the conclusion that the merger, as presented, with its detriments, its "striking disparity" of benefits and (*a fortiori* but not defined) its ancillary deeply injurious registration rights agreement, was properly held to be a transaction not within the terms of Section 17(b), and that the ruling of the Commission that The Investment Company Act of 1940 created a safe haven as a matter of law so that a closed end Investment Company which has a fiduciary relationship with and controls an affiliated company can force a merger without allowing the controlled company to share in vast benefits and increments its forced consent makes possible, was erroneous and properly found so by the Court below.

This unique case, unless the reversal of the Court below stands, can only create mischief and endless distinctions on its special facts in future Section 17(b) applications. This is a kind of a matter that under all the circumstances should be laid to rest so that in the future, as in the past, fairness will be determined on various factors so aptly catalogued by DuPont's counsel (App. 53a, f. 12).

It is respectfully submitted that the petitions for writs of certiorari should be denied.

Respectfully submitted,

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APPENDIX I.

EXCERPTS FROM FINANCIAL STATEMENT
(C. A. APP. 715, 7, 8)

CHRISTIANA SECURITIES COMPANY
BALANCE SHEET
(DOLLARS IN THOUSANDS)

ASSETS

	June 30, 1972	December 31, 1975
Investments (Note 6):		
E. I. duPont de Nemours and Company:		
Common—13,417,120 shares	74,621.9	74,621.9
Preferred, $4.50 cumulative —16,256 shares.	1,298.1	1,298.1
Wilmington Trust Company, common—69,216 shares	903.6	903.6
The News-Journal Company (wholly-owned), common—7,460 shares	846.1	846.1
Total investments	77,669.7	77,669.7

NOTES TO FINANCIAL STATEMENTS
(DOLLARS IN THOUSANDS, EXCEPT PER SHARE)
(EMPHASIS SUPPLIED)

3. Unrealized Appreciation on Investments

The following amounts for unrealized appreciation on investments are computed *by subtracting the carrying values from the amounts obtained by multiplying the number of shares of the various investments by the respective quoted market prices* at the indicated dates (except the appraised value of $24,296.0 for the investment in The News-Journal Company applied retroactively for all applicable periods—see Note 6) and without regard to any effect of such unrealized appreciation on future Federal income tax liability. *The amounts so computed are not represented to be realizable values for blocks of shares of the magnitude held.*

	June 30, 1972	December 31, 1971	December 31, 1970	December 31, 1969
Balance beginning of period	$1,895,819.5	$1,740,017.5	$1,359,258.0	$2,165,213.1
Balance end of period	2,150,851.6	1,895,819.5	1,740,017.5	1,359,258.0
Increase (decrease) during the period	$ 255,032.1	$ 155,802.0	$ 380,759.5	$ (805,955.1)

6. Investments

The carrying value of each of the investments in capital stocks is the same as the basis for Federal income tax purposes.

The quoted market price per share of investments at June 30, 1972 and December 31, 1971 and the amounts obtained by multiplying such prices by the number of shares on those dates were as follows:

	June 30, 1972		December 31, 1971	
	Quoted Market Price Per Share	Shares Owned Times Price Per Share	Quoted Market Price Per Share	Shares Owned Times Price Per Share
E. I. duPont de Nemours and Company:				
Common	$164.00	$2,200,407.7	$145.00	$1,945,482.4
Preferred	71.00	1,154.2	69.75	1,133.9
Wilmington Trust Company, Common	39.00	2,154.2	37.75	2,612.9
The News-Journal Company, Common	(a)	—	(a)	—

The amounts computed as shown above are not represented to be either the aggregate quoted market or realizable values of the respective investments.

7. NET ASSET COVERAGE AND NET ASSET VALUE

The following sets forth the net asset coverage per share of preferred stock and the net asset value per share of common stock outstanding at June 30, 1972 and December 31, 1971, *computed as to the valuation of investment securities on the basis of multiplying the number of shares of the various investments by the respective quoted market prices per share at those dates* (except for an aggregate of $24,260.0 for the investment of The News-Journal Company applied retroactively at both dates—see Note 6) *and including such unrealized appreciation of investments without regard to any effect thereof on furture Federal income tax liability*:

	June 30, 1972	December 31, 1971
Net asset coverage per share of preferred stock, 106,-500 shares outstanding .	$21,091.32	$18,681.79
Net asset value per share of common stock, 11,710,-103 shares outstanding:		
On basis of preferred stock having a liquidation value of $100 a share	$ 190.91	$ 169.00
On basis of preferred stock having a redemption value of $120 a share	$ 190.73	$ 168.81

APPENDIX II.

8. THE MERGER TERMS ARE PATENTLY NOT BALANCED AT ALL AND ARE UNFAIR ON THEIR FACE

Using pre-merger talk figures, this is what the Opinion and Order sanctions:

Christiana Shareholder Gets	DuPont Shareholder Gets
$41.25 in added *available* price of investment (close to half billion dollars)	$1.10 increase in equity per share (80 cents net) (Not an *available* sum to shareholders.)
7.2% increase in dividends.	3 cents increase in share of earnings. $7.34 vs. $7.31 per 1971 figures (Also not available)
Liquidity (Opportunity to cash in marketable shares.)	No increase in market value
Registration rights. (Not available to unaffiliated shareholders.)	Loses:
¼ free of restrictions for unaffiliated shareholders.	Effect of Market Impact of added shares. Affects DuPont as a company as to shares issued in acquisition or in new financing, and also all stockholders who sell.
Tax free liquidation result.	Surrendered responsibility of directors to be guided by DuPont's interests from time to time in regard to Registration.
Operating cost elimination .3%	Management responsibility to shareholders interest underwritten by Christiana's centralized shareholder interest in DuPont's operation and possibility of effectively protecting DuPont shareholders from poor management.
Relinquishes:	
(Transfers)	
Voting Control	

DuPont Management Gets
Control*

* Except it surrenders control of registrations.

APPENDIX III.

Comments on Harriman v. *DuPont*

With reference to the opinion in the case of *Harriman* v. *DuPont*, (D. Del. 12/23/75) now published at 411 F. Supp. 133, which is referred to in the D-C Petition, a substantial portion of the opinion being included in its appendix, there is this to be said: The record in the Eighth Circuit includes a rather extensive "Application for a Stay of the Order of the Securities and Exchange Commission Pending the Results of the Review in the Eighth Circuit." The lack of such a stay or a pending Application therefor was the original reason given by the District Court for going ahead with the trial that would have been mooted if the SEC exemption had been, as it was, reversed. Subsequently, the same reason was given for not delaying issuing an opinion and order. This was the reason for the Application for a stay by this Respondent, who was also co-counsel for the Delaware plaintiffs. The several grounds urged for a stay and for the Delaware District Court not dealing with this matter are apparent from the petition but undoubtedly too detailed for this filing. Subsequent to the entry of the Eighth Circuit Court Opinion and an Order, in one of the filings for DuPont and Christiana, in opposition to plaintiffs' motion to alter and amend the order and the opinion of the Delaware District Court, in view of the Eighth Circuit Court's ruling, which, if final, made the transaction impossible, the corporate petitioners here (and the defendants there) filed an answer as follows:

> "The issues that have been resolved by this Court were not before the Eighth Circuit and are not touched by its decision. This Court determined, after trial, that the terms of the proposed merger in no way violate the laws of Delaware and provide no basis for an action under Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder. The Eighth Circuit recognized that its decision did not purport to deal with either of these issues (Slip Op. 26, fn. 18; 32, fn. 23), and this Court's opinion specifically notes that 'the issues before this Court and the Eighth Circuit are separate and distinct' (Op. 38, fn. 109)." (See also footnote 131 at the D-C Petition Appendix Page 2a.)

The Eighth Circuit did not choose to act on the application for a stay and the Delaware District Court judge did not originally choose to delay until the Eighth Circuit acted. However, the Eighth Circuit Court Opinion was soon thereafter rendered while the Motion to Alter and Amend was still pending and the Delaware District Court judge did vacate the final judgment under Rule 54(b) deciding Delaware law and Rule 10b5 issues (which reserved matters as to a future proxy), and entered a nonappealable general judgment on the issues raised by the pleadings with a like reservation, and with no statement as to finality. It goes without saying that this nonappealable judgment of the District Court is only an interim one and does not rise to the dignity of a counter-authority on the issues presented (as the D-C Petition now ambivalently chooses to use it, while previously protesting its inapplicability). Since both courts explicitly walked wide of each other via the two footnotes in each opinion, the footnotes should be taken in good faith, and any relevant bearing here of the language of the Court quoted in the D-C Petition Appendix as offered here was rendered on a matter which the Court had no jurisdiction and is an obvious usurpation of and intrusion upon the role that the Eighth Circuit had under Section 43(a) of the 1940 Act, which gave it exclusive jurisdiction to review the order of the Commission granting exemption and to find the facts and law applicable in judging fairness under the 1940 Act as well as the other stipulations of Section 17(b). (The SEC is not a party to the Delaware proceeding.)